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Supreme Court of the United States

OCTOBER TERM, 1957

No. 146

UNITED STATES OF AMERICA, PETITIONER,

versus

HOWARD A. McNINCH, d/b/a THE HOME COMFORT CO., ROSALIE McNINCH AND GARIS P. ZEIGLER; FREDERICK L. TOEPLEMAN; AND CATO BROS., INC., WILFRED R. CATO, WILLIAM R. CATO, AND MAGIE L. DUNN (NEE: MAGIE L. STONE).

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF FOR HOWARD A. McNINCH, ROSALIE McNINCH AND GARIS P. ZEIGLER

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QUESTION PRESENTED

Whether appellees, Howard A. McNinch, Rosalie McNinch and Garis P. Zeigler, made, or caused to be made, or presented, or caused to be presented, for payment or approval, to the United States, or any department or officer thereof, any claim upon or against the Government of the United States within the contemplation, intent or purview of the Civil False Claims Statute.

STATUTES INVOLVED

The False Claims Act is composed of Sections 3490 and 5438 of the Revised Statutes of 1878. Section 3490 is a civil statute whereas Section 5438 is a criminal statute. Section 3490 (the Civil False Claims Statute), has never been amended although the criminal statute (R. S. 5438), has been amended.

The language of the Civil False Claims Act is to be found in Section 3490, Revised Statutes of 1878, and is as follows:

> "Any person not in the military or naval forces of the United States, or in the militia called into or actually employed in the services of the United States, who shall do or commit any of the acts prohibited by any of the provisions of section fifty-four hundred and thirty-eight, Title 'Crimes', shall forfeit and pay to the United States the sum of Two Thousand Dollars, and, in addition, double the amount of damages which the United States may have sustained by reason of the doing or committing such act, together with the costs of suit; and such forfeiture and damages shall be sued for in the same suit."

Prior to the amendment of R. S. 5438 (the criminal statute), the pertinent portion of that section, incorporated by reference in R. S. 3490, was as follows:

> "Every person who makes or causes to be made, or presents or causes to be presented, for payment or approval, to or by any person or officer in the civil, military, or naval services of the United States, any claim upon or against the Government of the United States, or any department or officer thereof, knowing such claim to be false, fictitious, or fraudulent, or who, for the purpose of obtaining or aiding to obtain the payment or approval of such claim, makes, uses or causes to be made or used, any false bill, receipt, voucher, roll, account, claim, certificate, affidavit, or deposition, knowing the same to contain any fraudulent

or fictitious statement or entry, or who enters into any agreement, combination, or conspiracy to defraud the Government of the United States or any department or officer thereof, by obtaining or aiding to obtain the payment or allowance of any false or fraudulent claim, * * * shall be imprisoned at hard labor for not less than one nor more than five years, or fined not less than one thousand nor more than five thousand dollars."

STATEMENT OF THE CASE

The relevant facts, which are not disputed, can be summarized as follows:

The Appellee, Howard A. McNinch,* was President, the Appellee, Mrs. Rosalie L. McNinch, was Secretary, and the Appellee, Garis P. Zeigler, was salesman of an unincorporated home construction business located in Columbia, South Carolina.

From November 6, 1951 to January 10, 1953, Appellees presented to The South Carolina National Bank, a FHA approved lending institution, eleven false FHA credit loan applications in connection with home improvement loans. The loans were sought on behalf of home-owner customers for the purpose of financing such improvements, each application was also accompanied by a fictitious credit report. Both the applications and reports misrepresented the financial eligibility of the customer for the insured loan.

The South Carolina National Bank, a private lending institution, made the loans as requested and the same were insured routinely by the FHA as a property improvement loan, insurable under Title 1 of the Federal Housing Act.

The FHA acknowledged the loans for insurance and billed the bank for the premiums required by the act.

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* The Appellee, Howard A. McNinch, died in September, 1955, and since that time the Appellee, Rosalie L. McNinch, has been duly appointed as the legal representative of his estate.

Prior to this proceeding Appellees, Howard A. McNinch and Garis P. Zeigler, plead guilty of violating 18 U. S. C. 1010, which prohibits making false statements for the purpose of obtaining FHA insured loans. The Appellee, Howard A. McNinch, before this ateion or the criminal action were commenced had purchased all the outstanding FHA insured loans and mortgages and assigned them to the bank for collection, and as a result thereof no claims can ever be made against the FHA under their insurance contract.

SUMMARY OF ARGUMENT

The Government contends that the appellees are liable in the amount of two thousand ($2,000.00) dollars for each of the eleven FHA Credit Loan Applications by reason of the provisions of the Civil False Claims Act.

Thus, the sole question for decision is whether what the appellees did constituted a violation of this false claims statute.

The United States in an elaborate and ingenious argument contends that the False Claims Act must be liberally construed so as to provide protection against those who would "cheat the United States." In substance, the Government's theory is that the appellees, in furnishing to the lending bank false credit information with reference to the borrower thereby made a claim upon the Government for an extension of its credit in support of the loan applied for, as a result of which the Government was cheated and this was in effect a false claim in which the United States was fraudulently induced to part with money or property, within the meaning of the Civil False Claims Statute.

Appellees contend (1) that the appellees did not present a claim against the Government of the United States within the meaning of the Civil False Claims Statute, and (2) that a false claim against the Federal Housing Admin-

istration is not a false claim against the Government of the United States within the meaning of Section 5438 of the Revised Statutes of 1878.

ARGUMENT

I

The Acts prohibited by the False Claims Act must be given careful scrutiny unless those be brought within its terms who are not clearly included.

The Government here, as it did in *United States v. Cochran*, 235 Fed. (2d) 131, Certiorari denied, 352 U. S. 941, and *United States v. Tieger*, 234 Fed. (2d) 589, Certiorari denied, 352 U. S. 941, stresses "the need for a functional interpretation" of the False Claims Act, so as to provide protection against those who would "cheat the United States", and cites *United States ex rel. Marcus v. Hess*, 317 U. S. 537, 87 L. Ed. 443, in support thereof.

Implicit throughout the Government's argument is the thesis that the False Claims Act should be given a liberal and expansive interpretation.

The petitioner severely criticizes the "penal" construction philosophy which finds expression in the majority opinion in the *Cochran case, supra.* (235 Fed. (2d), at page 133.) As we have already pointed out the Civil False Claims Statute incorporates by reference the provisions of the original Criminal False Claims Statute. (R. S. 5438.) As is clearly indicated by the decision in the *Hess case* this Court determined that which constituted a violation of the criminal statute also constituted a violation of the civil statute. This being so we submit that in construing the statute in question the Court is certainly dealing with the scope of a criminal statute. In the *Hess case*, so heavily relied upon by petitioner, this Court, in speaking of the construction to be given to Sections 3490 and 5438, said:

"* * * And we cannot say that the same substantive language has one meaning if criminal prosecutions are brought by public officials and quite a different meaning where the same language is invoked by an informer." (317 U. S. at page 542.)

And also:

"Sound rules of statutory interpretation exist to discover and not to direct the Congressional will. True, Sec. 5438 is criminal and for that reason in interpreting so much of its language as it shares in common with Sec. 3490 we must give it careful scrutiny lest those be brought within its reach who are not clearly included; but after such scrutiny we must give it the fair meaning of its intendment." 317 U. S., at page 542.

It is thus apparent that the Court in that case held that the particular facts therein involved brought the subject matter within the purview of both the criminal and the Civil False Claims Statutes, saying that Act should be given "the fair meaning of its intendment", which, incidentally, was "to provide protection against those who would cheat the United States." This language was obviously used with reference to a factual situation which clearly fell within the terms of the False Claims Statute and this Court did not mean to say, as the Government contends, that the False Claims Statute was intended to cover every situation where someone might intend to cheat the United States even though what that person did was not clearly included within the reach of the False Claims Statute.

The Government's argument that the False Claims Act must be construed to provide protection against all those who would "cheat the United States, "based upon general and isolated quotations from the *Hess case*, either overlooks or disregards the oft-repeated admonition of Chief Justice Marshall "that general expressions, in every opinion, are to be taken in connection with the case in which

these expressions are used," and if they go "beyond the case, they may be respected, but ought not to control the judgment in a subsequent suit when the very point is presented for decision." *Cohen v. Virginia*, 6 heat 264, 399, 19 U. S. 264.

The Government's reliance upon the decision of the Supreme Court in *Rex Trailer Company, Inc., v. United States*, 350 U. S. 148, like its reliance upon the *Hess case*, is based on certain language in the opinion where the Court was dealing with an entirely different factual situation.

Apparently the Appellants in the *Rex Trailer case* were prosecuted and convicted of a violation of Title 18, Sec. 1001 U. S. C., which is dissimilar from the False Claims Act and broader in scope, in that it does not require the filing of a false claim, but covers the making of any false, claim, but covers the making of any false, fictitious or fraudulent statement or representation.

The statement in Mr. Justice Clark's opinion in the *Rex Trailer case* to the effect that the *Hess case* "involved a provision of the False Claims Act * * * essentially the equivalent of Section 26(b)(1) (of the Surplus Property Act of 1944, 50 U. S. C. A. Sec. 1635) * * *", obviously refers to the civil remedies provisions of the two acts, which are essentially equivalent. We say it is obvious because the Court was considering the contention that the application or allowance of the civil remedies provisions would constitute double jeopardy with reference to a person who had been previously indicted and convicted for defrauding the Government in connection with the same transaction.

As appears from the decision of the Seventh Circuit in *United States v. Rex Trailer Company, Inc.*, 218 F. (2d) 880, 882, Section 26(b) of the Surplus Property Act of 1944, now Title 40, Sec. 489, U. S. C., which grants to the

United States several remedies similar to those provided by the False Claims Act, was enacted by Congress shortly after the decision of the Supreme Court in *United States ex rel. Marcus v. Hess, supra.*

The Respondents Howard A. McNinch and Garis P. Zeigler were indicted and prosecuted under the applicable statute, Section 1010, Title 18, U. S. C., for in making false statements in connection with securing loans from the lending bank.

The provisions of Section 1010, Title 18, U. S. C. are as follows:

> "Whoever, for the purpose of obtaining any loan or advance of credit from any person, partnership, association, or corporation with the intent that such loan or advance of credit shall be offered to or accepted by the Federal Housing Administration for insurance, or for the purpose of obtaining any extension or renewal of any loan, advance of credit, or mortgage insured by such Administration, or the acceptance, release, or substitution of any security on such a loan, advance of credit, or for the purpose of influencing in any way the action of such Administration, makes, passes, utters, or publishes any statement, knowing the same to be false, or alters, forges, or counterfeits any instrument, paper, or document, or utters, publishes, or passes as true any instrument, paper, or document, knowing it to have been altered, forged, or counterfeited, or willfully over values any security, asset, or income, shall be fined not more than $5,000.00 or imprisoned not more than two years, or both."

It would seem clear that Congress deemed the Criminal False Claims Statute to be inapplicable to persons who make false or fraudulent statements in connection with procuring an F. H. A. loan, for otherwise there would have been no reason for the adoption of Section 1010.

It is obvious that Section 1010 is much broader in scope in that it includes persons who do not come within the

False Claims Act. Section 1010 does not deal with persons who make claims against the F. H. A., but is designed to punish those who make false statements in connection with any application for an F. H. A. loan. In other words, it is clearly applicable to what these appellees did in this case whereas the False Claims Statute is not.

The fallacy in the Government's position is pointed out in the majority opinion of the Fifth Circuit in the *Cochran case*, 235 Fed. (2d), at page 134, where it is said:

> "It goes without saying that the acts of the defendant were criminal and that he was correctly prosecuted and convicted under the applicable statute, Sec. 1010, Title 18, U. S. C., for making false statements in connection with procuring the loan from the bank. It is quite another thing, however, to say that, because he was so guilty, he was subject to the penalties provided in Section 231. Section 1010 does not so provide. It specifically denounces as an offense the making 'for the purpose of obtaining any loan or advance of credit from any * * * or corporation with the intent that such loan or advance of credit shall be offered to or accepted by the Federal Housing Administration for insurance * * * any statement knowing the same to be false', and under this statute, which plainly dealt with and plainly denounced his actions as an offense, defendant was correctly prosecuted and convicted.
>
> "What the government is in effect doing here is reading into Sec. 231, the language of Sec. 1010, or, putting it differently, reading Sec. 231 as though it contained the same or similar language to Sec. 1010, whereas, as plainly appears in note 1, *supra*, nowhere in it is there any language having such purport or effect. Every word and line of this statute breathes the purpose to deal, it has the effect of dealing, only with the acts of persons falsely claiming money or property in the circumstances and with the effect dealt with in the statute. The statute does not deal with or denounce fraud in general. It cannot be read as doing so. In the *Marcus case*, on which the government so

strongly relies, the court thus correctly states the rule controlling here:

"'Sound rules of statutory interpretation exist to discover and not to direct the congressional will. True Sec. 5438 is criminal and for that reason in interpreting so much of its language as it shares in common with Sec. 3490 we must give it careful scrutiny lest those be brought within its reach who are not clearly included; but after such scrutiny we must give it the fair meaning of its intendment.'"

II

No claim, within the contemplation, intent and/or purview of the False Claims Statute, was made, caused to be made, presented, or caused to be presented by these Appellees.

As stated in the majority opinion of the Third Circuit in *United States v. Martin Tjeger*, 234 Fed. (2d) 589, it would seem apparent that the False Claims Act can be applied to this case only if the Government's contractual undertaking to repay a private bank loan if the borrower should default, itself constituted the "payment or approval" of a "claim against * * * United States."

We believe the Court in that case has demonstrated that what the Appellees did in this case did not constitute a violation of the False Claims Act. It was there said:

"But whatever combination of words may seem most favorable to the government, the statute can apply to this case only if the government's contractual undertaking to repay a private bank loan if the borrower should default, itself constituted the 'payment or approval' of a claim against the * * * United States.' We think this is a fair and accurate statement of the government's legal problem. At the same time it reveals the inherent difficulty and weakness of the position the government has to take. For the conception of a claim against the government normally connotes a

demand for money or for some transfer of public property. Believing that connotation applies here, we shall affirm the judgment below simply on the ground that when Congress legislated against fraud in connection with the 'payment or approval' of 'any claim upon or against the * * * United States' it did not cover fraud in inducing the United States to make a guarantor's promise, performance of which was conditioned upon an event which never occurred. True, the contract Tieger induced might have led to what would undoubtedly be considered a claim against the United States, but it never did. And certainly, there is no indication that Tieger intended or even anticipated any default by the borrower and consequent claim on the guarantor.

"Actually, the alleged claim against the United States here is no more than the privilege of the lending bank, in such a case as the loan application falsely represented this to be, to negotiate a unilateral contract under which the bank pays a modest consideration and receives in return the promise of the United States to make good if a borrower shall default. It is possible to view this commercially advantageous privilege of exchanging a little money for such an aleatory promise as a claim. But this privilege of contracting certainly is not a claim in normal business or legal usage and terminology. For familiar example, a policy of life insurance often accords the owner during the life of the insured a privilege of converting the policy into a new different contract. It seems as strange to describe the exercise of this privilege of contracting as a claim, as it is normal so to denominate an application for the sum payable upon the death of the insured.

"Both the legislative history and certain language of the False Claims Act point to the soundness of the construction which thus restricts 'claim * * * against the * * * United States' to this convential meaning of demand for money or property. But resort to these is unnecessary because the Supreme Court has so clearly stated its view of the matter.

"*United States v. Cohn*, 1926, 270 U. S. 339, 46 S. Ct. 251, 70 L. Ed. 616, was a criminal prosecution in which one of the charges was the violation of the very provision now in suit, which then was effectuated and enforcible by a criminal as well as a civil sanction. Referring to this provision the court explicitly considered whether the conduct of the defendant amounted to 'obtaining the approval of a "claim upon or against" the Government, within the meaning of the statute (False Claims Act).' It then construed the decisive language of the statute, saying: 'While the word "claim" may sometimes be used in the broad judicial sense of "a demand of some matter as of right, made by one person upon another, to do or to forebear to do some act or thing as a matter of duty," *Prigg v. Commonwealth of Pennsylvania*, 16 Pet. 539, 615 (10 L. Ed. 1060), it is clear in the light of the entire context, that in the present statute, the provision relating to the payment or approval of a 'claim upon or against' the Government relates solely to the payment or approval of a claim for money or property to which a right is asserted against the Government, based upon the Government's own liability to the claimant.' 270 U. S. at 345-346, 56 S. Ct. at page 252.

"Seeking to minimize the force of this construction the government calls it 'dictum', meaning, apparently, that this construction was more restrictive than the exigencies of the case required. But, to an inferior federal court, such a plain statement of a statute's meaning, adopted by the Supreme Court as the basis of its decision is much more than 'dictum', however apparent it may seem to analysts that the court could have gone on a narrower ground, had it chosen to do so.

"The district court correctly concluded that the statute deals only with false claims upon the government for money or property and that no such claim is revealed in the counts which have been dismissed."

III

A false claim against Federal Housing Administration, an agency of the Government, is not a false claim against the Government of the United States within the meaning of Section 5438 of the Revised Statutes of 1878, and hence no penalties can be exacted under Section 3490 of the Revised Statutes of 1878.

This phase of the case is fully covered in the brief filed herein on behalf of the appellees *Cato Brothers, et al.*, and accordingly the arguments set forth in that brief are incorporated herein by reference.

The only difference between the status of Commodity Credit Corporation and that of the Federal Housing Administration, is that the former is wholly owned government corporation, acting as a governmental agency, whereas the latter is an unincorporated governmental agency having in reality essentially the same status as that of Commodity Credit Corporation and other federally owned corporations. The Commissioner of F. H. A. in carrying out his statutory duties is "authorized, in his official capacity, to sue and be sued in any court of competent jurisdiction, State or Federal." (12 U. S. C. 702.) F. H. A. has been made subject to the auditing and budgetary provisions of the Government Corporation Control Act. (31 U. S. C. 841 *et seq.*). Originally the funds for the operation of FHA were provided by the Government, but since July 1, 1940 the FHA has been self supporting and has paid all expenses out of earnings. From time to time it issues a report as to its financial status, just like any of the other Government corporations. On page 3 of the March 1, 1958 Report of the Federal Housing Administration the following appears:

> "Note: Since July 1, 1940, the FHA has been self-supporting and has paid all expenses out of earnings. In the early years of operation, the Treasury Department advanced funds totaling $65,497,433.00 to pay ex-

penses and to establish certain of the Insurance Funds. In the fiscal year 1954 all of the funds advanced were repaid to the U. S. Treasury together with interest thereon in the amount of $20,385,529.00."

CONCLUSION

For the foregoing reasons these respondents respectfully submit that the decision of the United States Court of Appeals for the Fourth Circuit in the *McNinch case* should be affirmed.

Respectfully submitted,

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